92 13 9307

O 87162
0-35812

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Form 10-Q

14/17
SR2-2264

(X) Quarterly report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended March 22, 1992, or
( ) Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from _____ to _____.

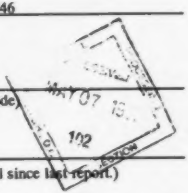
Commission file number 1-10111

SEA GALLEY STORES, INC.
(Exact name of registrant as specified in its charter)

Delaware	91-0838080
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

7116 - 220th Street S.W., Lynnwood, WA 98046
(Address of principal executive offices)

(206) 775-0411
(Registrant's telephone number, including area code)



(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No ___

As of March 22, 1992 the issuer had 3,284,786 shares of Common Stock outstanding.

L30

The Exhibit Index is on page 12 of this report.

1 of 14 pages in this report.

PROCESSED BY
14-14-V
MAY 12 1992

Microfilmed by
Q-Data Corp. - St. Petersburg, FL

PART I - FINANCIAL INFORMATION

SEA GALLEY STORES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 22, 1992	December 29, 1991
ASSETS		
Current assets		
Cash and equivalents	$ 126,000	$ --
Inventories	330,000	348,000
Accounts and notes receivable	216,000	273,000
Prepaid expenses	67,000	70,000
Assets held for resale	405,000	381,000
Total current assets	1,144,000	1,072,000
Property, equipment, and improvements, net of accumulated depreciation and amortization	5,644,000	5,765,000
Accounts and notes receivable	89,000	89,000
Certificate of deposit - restricted long-term	200,000	200,000
Other assets	2,311,000	2,402,000
	$ 9,388,000	$ 9,528,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 1,435,000	$ 1,515,000
Other current liabilities	11,086,000	10,726,000
Total current liabilities	12,521,000	12,241,000
Long-term indebtedness	5,297,000	5,115,000
Shareholders' deficit		
Common stock	199,000	199,000
Paid-in surplus	15,462,000	15,462,000
Deficit	(18,705,000)	(18,103,000)
	(3,044,000)	(2,442,000)
Less cost of common stock in treasury	(5,386,000)	(5,386,000)
Total shareholders' deficit	(8,430,000)	(7,828,000)
	$ 9,388,000	$ 9,528,000

See notes to condensed consolidated financial statements.

SEA GALLEY STORES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Twelve Weeks Ended March 22, 1992	Twelve Weeks Ended March 24, 1991
Net restaurant sales	$ 4,716,000	$ 4,988,000
Costs and expenses		
Cost of restaurant sales	3,860,000	4,072,000
Occupancy	686,000	906,000
Advertising and promotion	143,000	125,000
General and administrative	225,000	295,000
Other Expense, net	290,000	358,000
Loss before income taxes and discontinued operations	(488,000)	(768,000)
Provision for income taxes	-	-
Discontinued operation		
Loss from operations of discontinued subsidiary	(114,000)	(90,000)
Net loss	$ (602,000)	$ (858,000)

See notes to condensed consolidated financial statements.

SEA GALLEY STORES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Twelve Weeks Ended March 22, 1992	Twelve Weeks Ended March 24, 1991
Operating Activities		
Net loss	$ (602,000)	$ (858,000)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	231,000	357,000
Loss on disposition of assets	33,000	-
Provision for possible losses on repossession and dispositions	-	20,000
Distribution of stock held in treasury	-	13,000
Provision for severances	-	200,000
Changes in operating assets and liabilities:		
Decrease in inventories	18,000	32,000
Decrease in prepaid expenses	3,000	14,000
Increase in other assets	(1,000)	-
Increase (decrease) in trade accounts payable and accrued expenses	630,000	(174,000)
Decrease in other current liabilities	(40,000)	-
Net cash provided by (used in) operating activities	$ 272,000	$ (396,000)
Investing Activities		
Payments received on accounts and notes receivable	$ 586,000	$ 1,068,000
Acquisition of property, equipment, and improvements	(101,000)	(31,000)
Increase in accounts and notes receivable	(529,000)	(736,000)
Net cash provided by (used in) investing activities	$ (44,000)	$ 301,000
Financing Activities		
Proceeds from long-term borrowings and capital leases	$ 3,000	$ 3,000
Principal payments on long-term borrowings and capital leases	(105,000)	(188,000)
Payment of subordinated debt	-	(26,000)
Net cash used in financing activities	$ (102,000)	$ (211,000)
(Increase) decrease in cash and cash equivalents	$ 126,000	$ (306,000)
Cash and cash equivalents at beginning of year	-	378,000
Cash and cash equivalents at end of period	$ 126,000	$ 72,000

See notes to condensed consolidated financial statements.

SEA GALLEY STORES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE A -- SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation: The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions for Form 10-Q and do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. Certain prior year amounts have been reclassified to conform with current period presentation. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. However, the results of the first quarter are not necessarily indicative of the operating results of the full fiscal year. For further information, refer to the consolidated financial statements and footnotes included in the Company's Annual Report on Form 10-K for the year ended December 29, 1991.

Inventories: Restaurant inventories comprise food, liquor and supplies, and are stated at the lower of cost (first-in, first-out method) or market.

Going Concern: The Company's consolidated financial statements have been presented on a going concern basis which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. As more fully described under "Management's Discussion and Analysis of Results of Operations and Financial Condition," the liquidity of the Company has been adversely affected during the past several years by significant losses from operations primarily due to guest count declines, severance payments, write-down of assets and uneconomic long-term lease obligations. The Company has reported cumulative losses for the past three fiscal years of nearly $17 million (net loss for the year ended December 29, 1991 was $4.9 million) and, with a loss of $602,000 incurred during the first quarter, reported a shareholders' deficit of $8.4 million and a working capital deficit of $11.4 million at March 22, 1992. Additionally, the Company has defaulted on seven months' of interest payments on the subordinated debentures and is contingently liable under various lease obligations. These conditions raise substantial doubt about the Company's ability to continue as a going concern. The Company's continued existence is dependent upon achieving its 1992 operating plan to sustain increases in guest counts and sales and improve liquidity through debt restructuring.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND THE RESULTS OF OPERATIONS

General

As of March 22, 1992, Sea Galley Stores, Inc. (the "Company") operated 13 full service restaurants located in three northwestern states. The restaurants offer a moderately priced menu specializing in a wide variety of seafood entrees and a limited selection of fresh fish, meat, and poultry items. Substantially all of the restaurants emphasize semi-private seating and use a stylized nautical decor with rough plank walls, timbers, pilings, mock store fronts, and various other marine artifacts, such as rowboats, anchors, netting, life rings, and barrels.

Early in 1991, the NASD Board of Governors removed the Company's stock from the NASDAQ System due to the failure to meet net worth requirements. It is not anticipated that the Company will meet the net worth requirements to be re-listed in the foreseeable future. The stock is now listed on the OTC Bulletin Board.

Significant Litigation

The Company is involved in various legal proceedings, some of which may have a material impact on the future financial condition of the Company (see Part II, Item 1 - Legal Proceedings).

Liquidity and Capital Resources

The Company's cash position improved from no cash balances at December 29, 1991 to $126,000 at March 22, 1992, primarily as a result of deferring payments on trade payable and accrued expenses. The Company continued to incur operating losses during the first quarter of 1992, principally as a result of continuing bond interest costs, accrued but unpaid. The Company is experiencing a liquidity crisis, is currently in default on monthly bond interest payments due since the first of September, 1991 and does not anticipate making future interest payments. Under these circumstances, the trustee for the debenture holders has the right to accelerate the entire outstanding bond principal of $7,475,000. Additionally, the Company is seriously delinquent on certain secured debt and leasehold obligations pertaining to non-operating properties and, accordingly, is party to various associated legal proceedings (see Significant Litigation). These conditions raise substantial doubt about the Company's ability to continue as a going concern.

The Company remains current with most of its suppliers and obligations pertaining to operating restaurant properties. However, the Company does not anticipate that cash flow will be sufficient to pay past or on-going obligations relating to non-operating properties or the debenture obligations in accordance with the Indenture terms. As a result, the Company is considering various alternatives for restructuring its debt and obligations to enable it to maintain its core business.

Some of the alternatives the Company is considering include: (i) negotiating cash settlements of outstanding debts relating to non-operating properties; (ii) issuing amounts of equity for the cancellation of outstanding debt obligations; (iii) a recapitalization of the Company's subordinated debenture and other debt through a reorganization outside of bankruptcy; and (iv) a reorganization of the Company's debt and equity through a bankruptcy filing. The Company is actively pursuing settlements of on-going obligations as noted in items I and II above. Management is in regular communication with the trustee for the debenture holders who has refrained from accelerating the bond principal amount while management continues with negotiations and reorganization plans associated with alternatives (i) through (iii) above.

The Company continues to work diligently to sustain the increases in guest counts and sales and to improve gross margins. Management is attempting to accomplish this task through a refocused marketing effort and the promotion and fine-tuning of a new menu introduced late in the second quarter of 1991. The menu emphasizes lower priced, lower margin entrees that include the salad bar with each dinner selection. Because the Company's strategy emphasizes the offering of menu items with lower margins, guest counts and sales must increase substantially to provide the Company with profitable operations. Allowing such strategy sufficient time to more favorably impact guest counts and increase sales will require additional sources of working capital to fund operations.

The Company is pursing various avenues of opportunity to improve its liquidity. Some involve the sale and leaseback of the remaining owned restaurant properties while another pertains to the sell-off of a non-operating restaurant property. Management's plan to sell the remaining Ranch & Home site was compromised last year when benzene contamination of ground water was discovered at the site during the course of a routine environmental inspection pursuant to the terms of a pending sale agreement. The sale was never consummated and the land will require several years of remedial contamination clean-up before its eventual sale. Management is pursuing possible joint venture arrangements that will allow for leasehold development of the land and buildings at levels that will provide cash flows adequate to service underlying debt and associated overhead.

Management believes that the execution of the above plans will provide sufficient liquidity for the Company to continue as a going concern, and that the execution and realization of those plans is possible. Accordingly, the consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amount and classification of liabilities or any other adjustments that might be necessary should the Company be unable to continue as a going concern.

The Company has no material commitments for capital expenditures as of quarter-end and does not anticipate that any will arise throughout the remainder of the year.

Restaurant Operations

The Company operated during the current first quarter with four fewer operating units than were in operation throughout the first quarter of 1991. Accordingly, first quarter 1992 revenues fell to $4.7 million or 5.5% from the $5.0 million sales levels recorded during last year's first quarter. Sales

comparisons compiled for all stores open throughout both quarters (same-store comparisons) show that first quarter 1992 sales and guest counts increased 10% and 12%, respectively, when compared with the same values generated during the first quarter of 1991.

The following table sets forth components of cost of sales, gross restaurant profit and other restaurant expenses expressed as a percentage of restaurant sales.

	Twelve Weeks Ended March 22, 1992	Twelve Weeks Ended March 24, 1991
Net restaurant sales	100.0%	100.0%
Cost of sales		
Food and liquor	35.0%	35.1%
Labor	35.6%	35.9%
Other [1]	11.3%	10.6%
	81.9%	81.6%
Gross profit	18.1%	18.4%
Other costs		
Occupancy	14.6%	18.2%
Advertising and promotion	3.0%	2.5%
General and administrative	4.8%	5.9%
Other expenses	6.1%	7.2%
Loss from restaurant operations	(10.4)%	(15.4%)
Number of restaurants in operation	13	17

[1] Consists primarily of supplies, utilities and laundry.

Cost of restaurant sales, as a percent of sales, increased from 81.6% in the first quarter of 1991 to 81.9% for the 1992 first quarter. While modest efficiencies were achieved in the labor area, such gains were more than offset with increases in lounge promotion expenses classified as "other costs of sales."

Occupancy costs dropped substantially during the first quarter of 1992 primarily as a result of the 1991 disposition of restaurants with inordinately high occupancy expenses.

Marketing costs incurred during the 1992 first quarter increased slightly as a result of increased television advertising in smaller markets.

Reduced salary levels coupled with a relocation of the corporate offices to smaller, less expensive quarters resulted in a 24% reduction in general and administrative costs incurred during the first quarter of 1992 as compared with those costs incurred during last year's first quarter.

Other Expense, mostly comprising accrued bond interest expense, includes $21,000 in losses on disposition of company vehicles.

Other Events

The sublessee of an Iowa Sea Galley site defaulted on the sublease in 1990 and vacated the property in 1991. The Company was unable to remain current with the underlying lease obligations accruing at the rate of approximately $7,000 per month through November, 1997 and became subject to several judgments arising from the landlord's suit. Unpaid judgments subject to collection at December 29, 1991 aggregated approximately $55,000. In addition, another suit, which the Company contested, had been filed for approximately $40,000, essentially representing the remainder of the obligations accruing through fiscal 1991 year-end. Through first quarter garnishment proceedings, the litigant subsequently collected on the judgments. Company management has negotiated a settlement of this matter requiring an additional $57,000 to be paid monthly through November 1992. The settlement absolves the Company of all past, current and future obligations arising from the lease agreement.

In July 1989, the Company subleased two Colorado restaurants and a Wyoming restaurant to a former officer of the Company who continued to operate the facilities as Sea Galley restaurants under a Use of Name Agreement. The Company remained the primary obligor with respect to the underlying leases and, as such, continued to be liable in the event of default by the sub-tenant. During 1991, the sub-tenant defaulted on the Denver, Colorado obligations and the landlord sued the Company for performance under the lease agreement. The extent of obligations accruing to the Company at quarter-end amounts to approximately $149,000. On-going expenses accrue at a monthly rate of about $15,000. Management is working with the landlord to re-lease the property and to reach an acceptable settlement that removes the Company from any future obligations under a lease agreement that currently expires December 31, 2004. During the first quarter, the sub-tenant additionally defaulted on the Ft. Collins, Colorado lease and the landlord has served the Company with default notices. On-going expenses accrue at a monthly rate of approximately $9,000. As with the Denver property, Company management is working with the landlord to re-lease the property and to come to terms with an acceptable settlement that removes continuing liabilities under a lease agreement that currently expires January 31, 2004. The sub-tenant remains current under the Wyoming sublease obligations.

In October 1989, the Company sold its remaining five Colorado restaurants, all five of its Oregon restaurants and seven Washington restaurants to Kipper Acquisition Company, a wholly-owned subsidiary of Keg Restaurants USA, Inc. During the first quarter, Kipper abandoned all five of its Colorado properties and one property in Oregon. The Company has continuing leasehold obligations with four of the properties but is indemnified against losses by Kipper's parent company. Officials of Keg Restaurants USA, Inc. have provided Company management with absolute assurances that lease termination agreements will be structured to exclude Sea Galley Stores, Inc. from any past, present or future obligations.

The Company remains as the guarantor on one remaining Flakey Jake's lease. The tenant abandoned the property in December, 1991, leaving the lease in default as of year-end. The landlord has subsequently re-leased the property, subject to providing substantial tenant improvements, and served the Company with notices of defaults accumulating to approximately $120,000 as of quarter-end. Company management is vigorously contesting the default and believes that adequate defenses exist that will result in a reasonable accord.

The Financial Accounting Standards Board has issued Statements of Financial Accounting Standards No. 106 pertaining to post-retirement benefits, and No. 109, pertaining to accounting for income taxes. Companies are required to adopt these new methods of accounting no later than 1993. The Company does not intend to implement the Statements early. However, the adoption of these Statements is not expected to have a material impact on the Company's financial position.

Discontinued Retail Operations

In 1990, the Board of Directors authorized disposition of the American Ranch & home Supply Centers, Inc. subsidiary. Subsequently, two of the three retail outlets were sold. In accordance with its plan to liquidate the discontinued subsidiary, the Company continued in its efforts in 1991 to sell the remaining Ranch & Home store in Mount Vernon, Washington. During the fourth quarter an environmental inspection conducted in conjunction with a pending sale discovered benzene contamination of ground water at the site, thus terminating the sale. Management, anticipating that the property cannot be sold in the near future, is pursuing possible joint venture arrangements that will allow for leasehold development of the land and buildings on a piece-meal basis that will provide sufficient cash flows to service underlying debt and associated overhead.

The subsidiary lost $114,000 during the first quarter as thin margins from the modest sale of liquidation inventory fell far short of covering overhead costs.

Impact of Inflation and Regulation

The significant inflationary factors which have historically affected the Company results of operations include increases in the cost of food, liquor, and labor. Food costs are expected to continue to experience volatility in conjunction with the availability of key seafood and meat items.

Many of the Company's employees are paid hourly rates related to the federal minimum wage. Accordingly, increases in the minimum wage may occur and, consequently, increase the Company's labor costs. In this regard, effective April 1, 1991, Alaska and Idaho legislate increases in their state minimum wage rate of 10% and 12% respectively. Since the Company operates restaurants within these states, and with no "tip credit" provision similar to that allowed by federal minimum wage law, this legislation, combined with a related increase in payroll taxes, has an inflationary effect on labor costs and will have a continuing adverse impact on annual expenses of approximately $28,000 per year.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

In September, 1991, the Company was sued by Shifrin & Earle - III for breach of lease in the Colorado District Court for Denver County. The lawsuit arises from breach of a lease for a Sea Galley restaurant facility located in Aurora, Colorado. The Company subleased the property to Savannah's Restaurant of Denver, Inc. as part of a larger transaction in which it transferred three Sea Galley locations to an investor group. Savannah's went out of business in Denver and defaulted under the sublease. The landlord subsequently sued the Company and Savannah's for default under the lease. The complaint seeks damages of approximately $129,000 in past due rent and $19,735 in past due property taxes as of March, 1992; an additional $9,865 in property taxes will be due July 31, 1992. In addition, the plaintiff seeks to recover unpaid rent through the balance of the lease term, which expires on December 31, 2004, and is accruing at the rate of $13,000 per month. Finally, plaintiff seeks property taxes through the year 2004 at the rate of approximately $20,000 per year, as well as late charges and pre- and post-judgment interest. The Company has raised some defenses to the lawsuit which may result in some mitigation of the claimed amount. In addition, the Company has reached an interim settlement with the plaintiff pursuant to which it will pay plaintiff $7,500 per month and work with the plaintiff to lease the premises, and the plaintiff will dismiss the lawsuit without prejudice. The Company has located some potential tenants for the premises, and expects to reach a final settlement upon signing a lease.

In December, 1991, the Company was sued by Westdale Associates for breach of lease in the Iowa District Court for Linn County. This lawsuit alleges breach of the lease for the Sea Galley restaurant in the Westdale Mall in Cedar Rapids, Iowa. The Company subleased that restaurant location to a local operator in 1988. That operator went out of business and defaulted on the lease in 1990. The complaint seeks $39,933 in damages as well as recovery of unpaid rent, taxes, and common area maintenance charges, which accrue at the rate of $6,655 per month and will continue through November, 1997, the end of the lease term. Plaintiff filed a motion for summary judgment, which the Company defeated. The Company has reached a settlement with the plaintiff pursuant to which it will pay the plaintiff $57,151 over a seven month period in exchange for a satisfaction of judgment and a release from the lease.

In January, 1992, the Company was sued by Consumer Guaranty Corporation in the Superior Court of Arizona for Maricopa County. The claim arises out of the Company's default under a loan made by Sun State Savings and Loan Association to the Company for construction of a restaurant property in Mesa, Arizona. Sun State Savings subsequently went into bankruptcy, and the loan was purchased by the plaintiff. The property was subsequently sold through a sheriff's sale, and the subject lawsuit seeks recovery of the difference between the amount past due under the promissory note and the amount credited to the Company as a result of the sheriff's sale. The complaint seeks damages of approximately $200,000 plus interest, costs, and expenses. The Company has reached a settlement agreement pursuant to which it is obligated to pay plaintiff $100,000 in monthly installments of $5,000 commencing in May, 1992. Settlement documents are currently being prepared, and the Company expects that they will be executed in May, 1992.

In February, 1992, the Company was sued by Northridge Center for breach of lease in the Superior Court of California for the County of Los Angeles. The complaint alleges breach of a lease for a Flakey Jake's restaurant property outside of Los Angeles, California. The property was originally leased to Flakey Jake's, Inc., then a subsidiary of the Company, and Flakey Jake's obligations under the lease were fully guaranteed by the Company. Flakey Jake's was subsequently purchased by American Service Management Enterprises, which has defaulted on the lease. Plaintiff, landlord under the lease, is seeking unpaid rent and other amounts due under the lease, which total $68,782 as of December 9, 1991, and continue to accrue at the rate of $16,708 plus taxes and insurance through 2008. The Company has filed several defenses and counterclaims which may mitigate damages, and is also pursuing a cross-claim against American Services Management Enterprises. The Company intends to initiate settlement negotiations with the plaintiff regarding this lawsuit in the near future.

The Company was named as a defendant in litigation in the State of New Jersey in connection with a construction debris dump to which it allegedly contributed a small amount of debris. The dump caught fire, causing damage to a highway. The State of New Jersey cleaned it up, suing the owner and operator. The owner sued all the persons that hauled debris to the dump, including the Company. Total liability associated with the claim is, we understand, approximately $17,000,000. The Company has not engaged an attorney to evaluate or respond to the claim. The ultimate outcome of the litigation cannot be presently determined. Accordingly, no provision for any liability that may result upon adjudication has been made in the accompanying financial statements.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits:
(11) Statement of Computation of Earnings Per Share

(b) Reports on Form 8-K: None

EXHIBITS INDEX

Exhibit		Page
(11)	Statement of Computation of Earnings Per Share	14

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SEA GALLEY STORES, INC.

May 5, 1992
Date

By: Keith C. Huetson, Vice President, Treasurer and Chief Financial Officer

By: Jack E. Burton, Controller

Exhibit 11 - COMPUTATION OF EARNINGS PER SHARE

	12 Weeks Ended March 22, 1992	12 Weeks Ended March 24, 1991
Average shares outstanding	3,284,786	3,143,119
Net effect of dilutive stock options based on the treasury stock method using the greater of average or ending market price**	-	-
	3,284,786	3,143,119
Loss before discontinued operation	$ (488,000)	$ (768,000)
Loss from discontinued operation	(114,000)	(90,000)
Net loss	$ (602,000)	$ (858,000)
Loss per share:		
Loss before discontinued operations	$ (.15)	$ (.24)
Loss from discontinued operations	(.03)	(.03)
Net loss per share	$ (.18)	$ (.27)

**Calculation ignored as the effect on earnings per share would be antidilutive.